



Jennifer M. Granholm  
GOVERNOR

STATE OF MICHIGAN  
PUBLIC SERVICE COMMISSION  
DEPARTMENT OF LABOR & ECONOMIC GROWTH  
ROBERT W. SWANSON  
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J. Peter Lark  
CHAIRMAN

Laura Chappelle  
COMMISSIONER

Monica Martinez  
COMMISSIONER

June 2, 2006

Honorable Jennifer Granholm  
Governor of Michigan

Honorable Members of the Senate Technology and Energy Committee  
Secretary of the Senate

Honorable Members of the House of Representatives Energy and Technology Committee  
Clerk of the House of Representatives

The enclosed annual report, *Status of Telecommunications Competition in Michigan*, is submitted on behalf of the Michigan Public Service Commission in accordance with Section 103 of the Michigan Telecommunications Act as amended in November 2005. This report will be available on the Commission website at [www.michigan.gov/mpsc](http://www.michigan.gov/mpsc).

The purpose of this report is to describe the status of competition in telecommunications service in Michigan, including, but not limited to, the toll and local exchange service markets in the state. This report includes information on the traditional wireline industry as well as other telecommunications technologies. This is the sixth report of this nature.

During 2005, competition in the wireline telecommunications market in Michigan experienced the first decrease in the level of wireline competition since our monitoring began in 1999. In addition, 2005 marked the largest decrease in wirelines within the Michigan wireline market, falling 10.34% from 2004. The percentage of lines in the wireline market served by competitive providers is now at a 21.2% share, a 6.3% reduction from 2004. The decrease in the total number of competitive lines from 2004 to 2005 was 31%.

In 2005, the Federal Communications Commission (FCC) and the courts overturned portions of the FCC's Triennial Review Order in 2005, and eliminated the incumbents' obligation to provide UNE-P to the competitors at a regulated cost-based price. Competition for wireline basic local exchange service in Michigan, however, was mainly based on the competitors using local switching via AT&T's unbundled network element platform (UNE-P) to provision customers. Michigan's competitive market had been fostered due to vigilant regulatory oversight to ensure that competitors were able to obtain access to certain elements of the incumbent's network without incumbent interference or obstruction.

The competitors' transition away from UNE-P took place over 2005 and was completed on March 11, 2006. The Commission actively participated in the negotiations to transition customers in a timely and efficient manner. Competitive providers have transitioned customers from UNE-P to other methods; mostly using UNE-L provisioning which uses the competitors' switching or by using a product called Local Wholesale Complete (LWC) which competitors can purchase at non-regulated prices.

Due to a legislatively-imposed sunset, 2005 brought about a periodic review and change to the Michigan Telecommunications Act (MTA). On November 22, 2005, the new MTA was enacted which replaced state regulations with competition based on market forces. The only form of retail local service that remains subject to rate regulation is primary basic local exchange service (PBLES), which applies to residential voice customers, subject to limits of one line per household, no more than 100 outgoing calls per month, and no more than 12,000 outgoing minutes per month. The new MTA also made modifications to the resolution of disputes, alterations to Lifeline service, and maintained MPSC jurisdiction over quality of service matters and consumer protections.

The *Status of Telecommunications Competition in Michigan* report finds that the elimination of UNE-P as a more economical method of provisioning customers, the emergence of new technology options, and the recent mergers involving incumbents and competitors have led to the decrease in competition in the wireline industry in Michigan. It should be noted that these factors are governed by outside forces, such as the FCC and courts or are affected by the introduction of new technologies into the market, and are not under the direct regulatory control of this Commission.

The Commission will continue to strive to meet its obligations under the new MTA to ensure a reasonable PBLES rate, enforce basic consumer protections, including prohibitions against slamming and cramming, and resolve disputes that arise under the MTA. The Commission will also apprise the Governor and the Legislature of any future developments that may warrant action.

Sincerely,

J. Peter Lark, Chairman  
Michigan Public Service Commission

Laura Chappelle, Commissioner  
Michigan Public Service Commission

Monica Martinez, Commissioner  
Michigan Public Service Commission

# Status of Telecommunications Competition in Michigan

June 2006



Submitted by:  
**MICHIGAN PUBLIC SERVICE COMMISSION**  
Michigan Department of Labor and Economic Growth  
In Compliance with Public Act 179 of 1991 as amended

## **Introduction**

Section 103 of the Michigan Telecommunications Act (MTA), as amended in November of 2005 (MCL 484.2103), directs the Michigan Public Service Commission (Commission) to submit an annual report describing the status of competition in telecommunications service in Michigan, including, but not limited to, the toll and local exchange service markets in the state. A new provision of the MTA requires providers (except wireless carriers) to submit to the Commission all information necessary for the preparation of the annual report under this section.<sup>1</sup> This sixth report filed by the Commission includes information on the traditional wireline industry as well as other telecommunications technologies.

In 2005, the Federal Communications Commission (FCC) and the courts overturned portions of the FCC's Triennial Review Order in 2005, and eliminated the incumbents' obligation to provide unbundled network elements platform (UNE-P) to competitors at a regulated cost-based price. On November 22, 2005, the new MTA was enacted which replaced state regulations with competition based on market forces thereby creating only one form of retail local service subject to rate regulation. The *Status of Telecommunications Competition in Michigan* report finds that the elimination of UNE-P as a more economical method of provisioning customers, the emergence of new technology options, and the recent mergers involving incumbents and competitors have led to the decrease in competition in the wireline industry in Michigan.

## **Toll Markets**

The toll market is commonly referred to as long distance and the providers of such services are referred to as interexchange carriers (IXCs). IXCs that own their own facilities are

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<sup>1</sup> On January 10, 2006, the Commission issued an order in Case No. U-14749 which required all telecommunications providers in Michigan to provide the information needed to complete the report.

required to provide very little information to the Commission related to their operations. The Commission does not license IXCs and they are required only to file tariffs with the Commission that are consistent with the provisions of the MTA. IXCs providing toll service via resale<sup>2</sup> are exempt from this tariff filing requirement as well. As a result, there is limited information available regarding market share, customer numbers, or revenues for IXCs.

On May 1, 2000, the FCC Common Carrier Bureau issued an order in Docket No. 96-61 detariffing the interstate, domestic, interexchange services of nondominant IXCs. Detariffing means that long distance companies will no longer be required to file a document called a “tariff” for purposes of notifying the FCC about the rates, terms and conditions of long distance service offerings. The FCC concluded that detariffing would enhance competition among providers of interstate, domestic and interexchange services, and promote competitive market conditions. In 2001, after the transition period was completed, IXCs began providing service without filing tariffs with the FCC. They provide information to consumers via other means, such as their websites.

While the reselling of toll services is unregulated, the Commission has a registration process pursuant to MCL 484.2211a. Under this program, 183 carriers have registered as resellers of toll service in Michigan at the end of the first quarter of 2006. Although this is a self-registration process and is not subject to verification, nevertheless, it does indicate that there are numerous providers of this service. The Commission’s website provides a link for rate comparisons among providers. Additional information is available in the report of the FCC issued on June 21, 2005, *Trends in Telephone Service*. The FCC report indicates that from the end of 1999 to the present, the FCC has approved all the section 271 applications by the Bell Operating Companies (BOCs) to provide in-region interLATA service throughout the United

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<sup>2</sup> Resale is buying long distance phone lines in quantity at wholesale rates and then selling them to the end user for a profit.

States.<sup>3</sup> The FCC reports that more than 1,000 companies now offer wireline long distance service nationwide. These carriers remain subject to the FCC's jurisdiction. The FCC has chosen to rely on competition, rather than regulation, as much as possible. Thus, the FCC forbears from regulating most aspects of long distance service.

Effects of competition in the toll markets continue to be more evident in the number of optional toll package alternatives available, the number of providers who offer them and the declining prices for higher usage customers who do not utilize basic toll rates. Innovative bundling of services and new pricing plans are blurring the distinction between toll and local services. Many providers are offering unlimited local and long distance services, plus unregulated features, at one combined price. In some cases, these bundled services include wireless and internet access services, as well as satellite television.

### **Basic Local Exchange Market - Wireline**

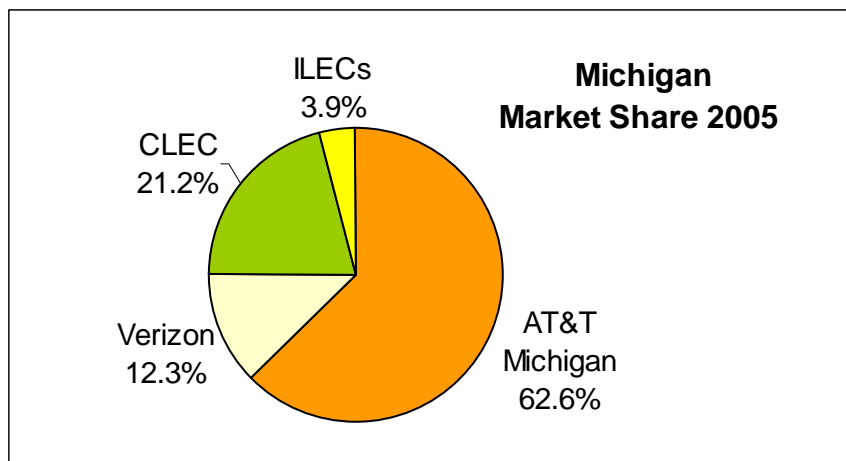
To obtain an accurate picture of the competitive marketplace in Michigan for basic local exchange service, the staff of the Commission has conducted annual surveys of AT&T Michigan (f/k/a SBC Michigan), Verizon, the smaller incumbent local exchange carriers (ILECs), as well as all licensed Competitive Local Exchange Carriers (CLECs) from 1999 – 2005. This survey includes ILECs that also operate as CLECs in Michigan. CLECs are providers that compete in the same geographic area as ILECs. This year's survey was sent out to 214 ILECs and CLECs in the state of Michigan that were licensed as of December 31, 2005. The data collected through this survey is for the year ended December 31, 2005. The information was gathered to assist the Commission staff in evaluating the scope of local competition in Michigan pursuant to Case No. U-14749.

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<sup>3</sup> Section 271 of the Federal Telecommunications Act of 1996 describes the conditions under that a Bell Operating Company (BOC) must satisfy to enter the market to provide interLATA services, long distance in particular, within the region where it operates as the dominant local telephone service provider.

The survey was originally developed through a collaborative process set forth in the Commission's order in Case No. U-12320. This docket was initiated to review SBC's (now AT&T Michigan) application for authority to provide in-region long distance service pursuant to Section 271 of the Federal Telecommunications Act of 1996. The survey for 2005 was updated and expanded to include other information relevant to the status of telecommunications competition in Michigan. Some of the information requested in the survey is considered confidential by the companies. Hence, the results of most portions of this survey are reported as total CLEC numbers to maintain the confidentiality of the individual company numbers. For 2005, all of the ILECs responded to the ILEC survey and 142 of the 188 CLECs and ILECs that have CLEC operations filed a response to the CLEC survey. From the group of CLECs, 78 reported that they are actually providing local service.

From the data compiled for 2005, staff found that the number of lines provided by



CLECs (including over their own facilities, through UNE-L,<sup>4</sup> UNE-P,<sup>5</sup> Local Wholesale Complete<sup>6</sup> (LWC), and through resale of incumbent providers services) was 1,158,550.

<sup>4</sup> UNE-L is an unbundled network element loop and is a common strategy used by facilities-based CLECs. A CLEC owns the local switch and leases the local loop from the ILEC. Unbundled network elements (UNEs) are defined as physical and functional elements of the network, e.g., Network Interface Devices, local loops, switch ports, and dedicated and common transport facilities.

<sup>5</sup> UNE-P is an unbundled network element platform or UNEs combined into a complete set in order to provide an end-to-end circuit.

<sup>6</sup> Local Wholesale Complete is AT&T Michigan's replacement offer for UNE-P, but at non-regulated rates.

The survey findings indicate that the total number of lines provided in Michigan (all ILECs including AT&T Michigan, Verizon and CLECs) was 5,471,708. CLEC lines accounted for 21.2% of the total lines in 2005. AT&T Michigan's share was 62.6% (3,423,548 lines) while Verizon's share was 12.3% (675,126 lines). The small independent telephone companies represented the remaining 3.9% (214,484 lines) of the total lines in Michigan.

The survey responses indicate that the geographic areas covered by CLEC lines continue to encompass primarily the Detroit, Grand Rapids, Lansing and Saginaw areas, with the majority of the competitive lines being provided in the Detroit vicinity. From the data that AT&T Michigan submitted, 62% of the competitive lines are provided in the Detroit area, 24% of the competitive lines are provided in the Grand Rapids area, 6% of the lines are provided in the Lansing area, 6% of the lines are provided in the Saginaw area, and 3% of the lines are provided in the Upper Peninsula area. It should be noted that most of the CLEC activity is in geographic areas that are served by AT&T Michigan. CLECs provide approximately 5% of the competitive lines in Verizon's areas.

The Commission continues to license new CLECs, and as of the end of 2005, the CLECs were providing service to 21.2% of the wireline lines provided to customers in Michigan. This is a decrease over the previous year and is the first decrease in the level of wireline competition since the staff began conducting the surveys seven years ago. On April 3, 2006, the FCC released its report on *Local Telephone Competition: Status as of June 30, 2005*. For the Michigan companies that are required to report this data to the FCC, the ILECs reported 4,409,360 lines, and the CLECs reported 1,473,461 for a total of 5,882,821 lines. From the most recent data available from the FCC, the CLEC share was reported at 26% as of June 30, 2005 which is consistent with this Commission's reported 2004 year end figure. This data gathered by



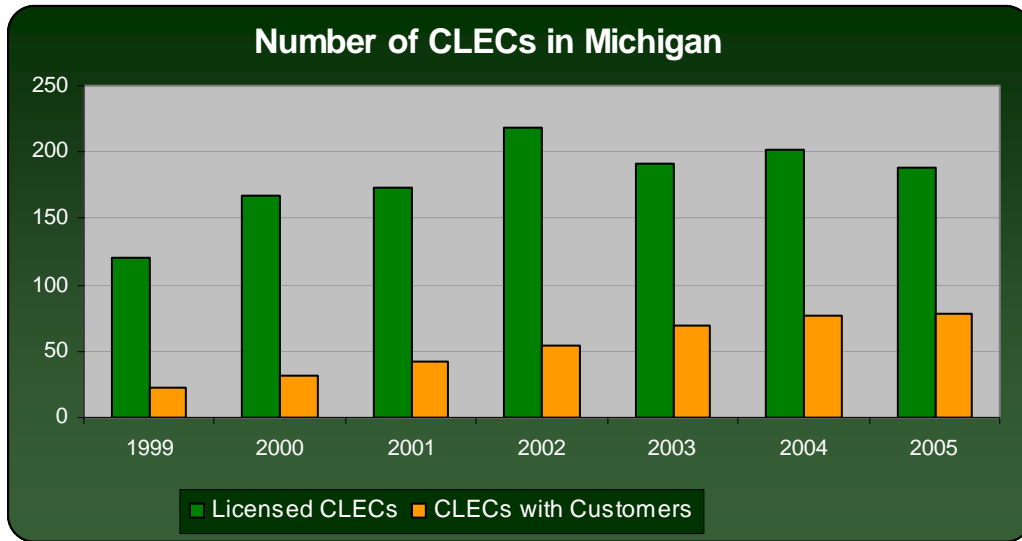
the FCC is from 7 reporting ILECs and 17 reporting CLECs in Michigan, representing the larger providers and a majority of the lines.

The following chart categorizes the CLECs according to the number of customer lines that they served in 2005. The data indicates that of the 142 CLECs reporting, 64 were serving no customers in 2005, which represents approximately 45% of the group, while the second group served between 1 line and 1,000 lines, a group of 31 CLECs or almost 22%. The third group served between 1,001 and 10,000 lines each and is comprised of 31 CLECs for a 22% share, and the last group of CLECs served over 10,000 lines each and represents 16 CLECs for an 11% share.

**The 2005 Michigan Survey Results Show That:**

CLECs With No Lines	64	45%
CLECs With 1 – 1,000 Lines	31	22%
CLECs With 1,001 – 10,000 Lines	31	22%
CLECs With over 10,000 Lines	16	11%
Total CLECs Responding to Survey	142	100%

The CLECs that report no line activity represent a number of licensed providers that are not yet providing service and have no tariffs filed or they are providing services other than local, such as resold long distance. The Commission has a process in place to review any license that is not actively being used over a reasonable period for revocation of the license.

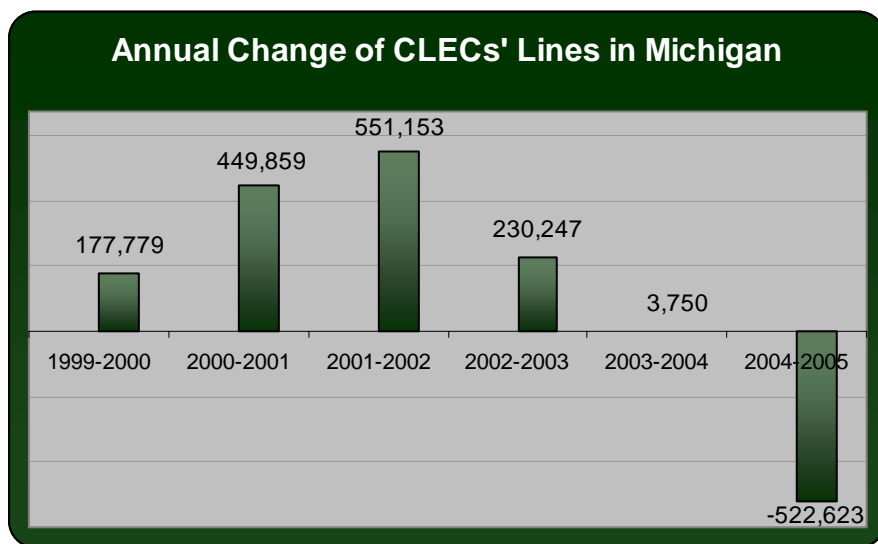


A portion of the data gathered by the Commission for the last seven years is presented below in table format.

### Michigan Public Service Commission CLEC Survey Results:

	1999	2000	2001	2002	2003	2004	2005
<b>Licensed CLECs</b>	120	167	173	219	192	202	188
<b>CLEC Responses</b>	59	69	102	113	112	127	142
<b>CLECs with Lines</b>	23	31	42	54	70	77	78
<b>CLEC Lines</b>	268,385	446,164	896,023	1,447,176	1,677,423	1,681,173	1,158,550
<b>Total Michigan Lines</b>	6,726,971	6,901,813	7,014,263	6,668,124	6,334,114	6,103,250	5,471,708
<b>CLEC %</b>	4 %	6.5 %	12.8 %	21.7%	26.5%	27.5%	21.2%
<b>AT&amp;T Michigan %</b>	81 %	78 %	72.2 %	62.9%	57.7%	56.9%	62.6%
<b>Verizon %</b>	11.5 %	12 %	11.5 %	11.9%	11.2%	11.8%	12.3%
<b>ILECs %</b>	3.5 %	3.5 %	3.5 %	3.6%	4.5%	3.7%	3.9%

As is shown, while total wireline lines have consistently decreased since 2001, the actual number of CLEC providers and CLEC lines in Michigan grew over the first six years that this information was gathered; the CLEC market grew from a 4% share to a 27.5% share at the end

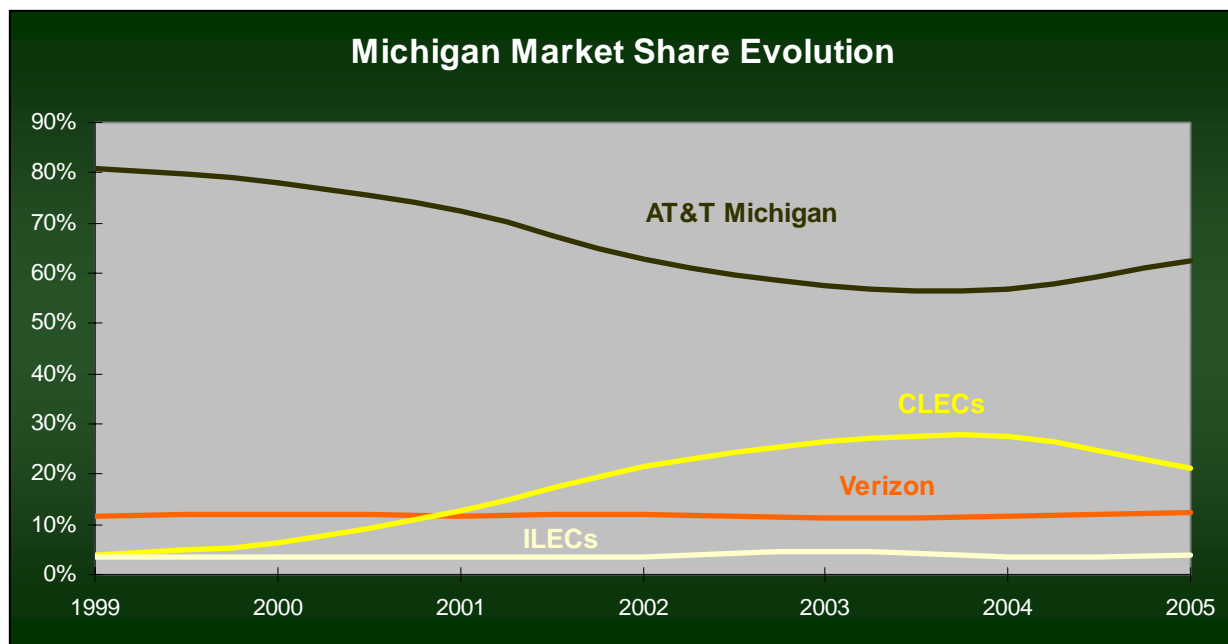


of 2004. However, for 2005, Michigan experienced the first ever decrease in CLEC lines since the Commission began conducting the surveys. There was a loss of 522,623

competitive lines in 2005, a 6.3% decline in the competitive market share from 2004, as well as a 31% reduction in the number of competitive lines.

The following graphical representation depicts the evolution of the market share over the last seven years. The chart indicates growth for the CLECs during the first six years while at the same time declining market share for AT&T Michigan. However, for 2005, CLEC lines decreased while market share for AT&T Michigan grew slightly. The market share for the small ILECs and Verizon remained fairly constant over the seven year period. Also of interest is that in 2005, the total number of customer wireline lines decreased, a trend that began in 2002, reflecting a continued loss to mobile wireless and other types of telephony including voice over internet protocol<sup>7</sup> (VOIP) as well as a movement away from using dial-up internet to high speed connections.

<sup>7</sup> VoIP is the technology used to transmit voice conversations over a data network using the internet protocol.

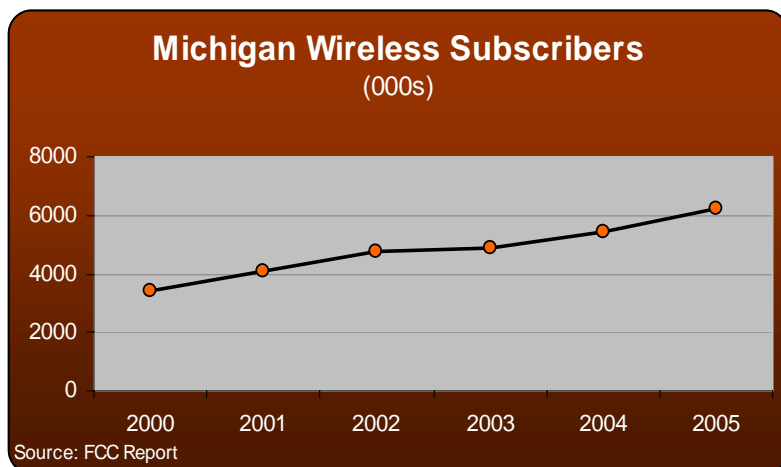


## Wireless Market

In preparing this report, the Commission did not obtain data from the wireless providers because under the MTA, wireless providers are not subject to the Commission's jurisdiction. Consequently, for purposes of preparing this report the Commission had to rely on wireless data obtained from the FCC.<sup>8</sup>

While the Commission does not regulate mobile wireless providers, we are monitoring the growth in this market as it pertains to competition for wireline phone service. The FCC prepares an annual report on *Local Telephone Competition: Status as of June 30, 2005* which includes data from mobile wireless companies serving in Michigan. According to this data 12 carriers reported offering wireless service in Michigan in 2005. The number of subscribers in Michigan has grown considerably over the past five years. In June of 2005, Michigan had 6,241,892 mobile wireless subscribers, an 80% increase over the 3,423,535 subscribers in 2000. There were 811,255 additional subscribers added from June 2004 to June 2005.

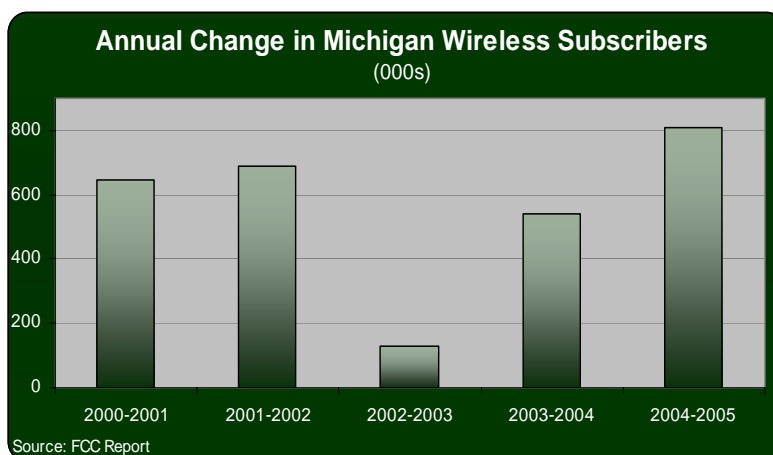
<sup>8</sup> While this report discusses the potential impact of the wireless market on wireline competition, it is not the contention of the Commission that mobile wireless service is a functional equivalent of fixed wireline service.



The FCC data indicates that the annual growth in this area of the telecommunications market has been consistently strong. Except for 2002 to 2003, there was an increase of over 500,000 subscribers each year

between 2000 and 2005. The largest annual increase in subscribers appeared from 2004-2005.

The recent increase shows that the market for mobile wireless phones is still growing in Michigan and may indeed be having stronger effects on telecommunications competition than in previous years, especially as mobile wireless carriers offer added features such as internet and video.



## **Emerging Technologies**

The Commission continues to monitor the development of emerging technologies in the broadband realm such as VoIP, Wi-Fi<sup>9</sup> technology, Wi-Max<sup>10</sup> and broadband over power lines<sup>11</sup> (BPL). The Commission opened an investigation into VoIP on March 16, 2004 and issued an

<sup>9</sup> Wi-Fi is a marketing phrase that is short for wireless fidelity. Wi-Fi uses an over-the-air interface between a wireless client and a base station, or between two wireless clients, that is often used to connect computers to the internet in airports, hotels and coffee shops.

<sup>10</sup> Wi-Max, which stands for Worldwide Interoperability for Microwave Access, can carry data at a potential speed of 70 million bits per second in a radius of up to 31 miles.

<sup>11</sup> Broadband over power lines refers to technologies for using electric utility companies' power lines to deliver broadband services.

order on April 28, 2005 recommending that the legislature amend the MTA so as to specifically empower the Commission to assess the effect of VoIP service on Michigan citizens. The MTA was amended in November 2005 to add a registration requirement for providers of new or emerging technologies. The Commission supports emerging technologies introduced into the market, as long as these new technologies do not harm the existing public switched network or its customers. Some of the issues related to VoIP and other new technologies include their impact on the federal universal service fund, 9-1-1 emergency calling capabilities and compensation among providers. These issues are all being debated on the national level.

Pursuant to the November 2005 amendments to the MTA, a general survey was sent to the VoIP providers registered in the Intrastate Telecommunications Service Providers (ITSP) registry. There are only a very small number of customers using VoIP services through these registered providers. About half of the responding companies currently offer services in Michigan including various combinations of local, long distance, and international calling. All of the responding providers who currently offer service indicated that their customers are able to access 911 services.

The registration for VoIP providers is a new requirement for 2006 and as such the Commission will be reviewing this area to ensure that all providers are compliant with the ITSP registry. Several CLECs also report that they provide VoIP services. In addition, AT&T Michigan and Verizon indicate they provide VoIP services through separate unregulated subsidiaries. Many of these providers offer service anywhere broadband connections are available although local number availability varies with the different providers. Since the obligation for VoIP providers to register with the Commission was imposed in 2005, there is insufficient data for the Commission; however, the Commission expects to have more information in 2006. At this time, the Commission is not able to determine if VOIP is a

significant competitor to wireline telecommunications in Michigan for 2005, although it is being actively marketed.

Many new technologies including VoIP require the use of broadband connections. These high-speed connections are available in many formats including DSL, cable, and wireless

technologies. According to the

most recent FCC data in the report

titled *High-Speed Services for*

*Internet Access: Status as of June*

*30, 2005*, Michigan residents and

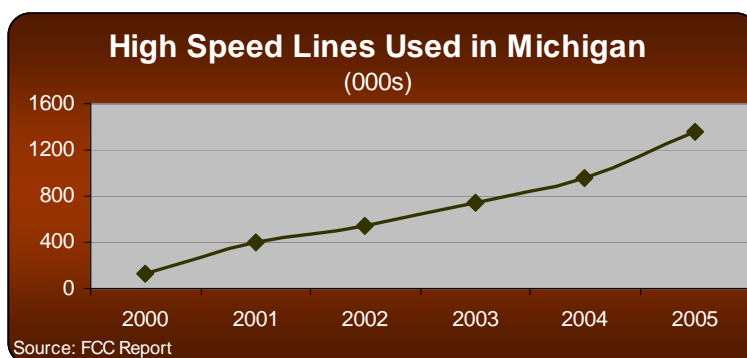
businesses used 1,359,079

high-speed<sup>12</sup> lines. As Michigan works to bring broadband access to an increasing number of

customers we can expect to see more growth in many of these new technologies.

An emerging technology in the broadband realm has been WiFi. WiFi hot spots have increasingly been deployed in this state. The independent private business initiative began as an added service in order to attract consumers primarily in coffee shops, hotels and airports. The realization of the need “to be connected” has motivated many government entities to consider offering WiFi; such is the case with several state parks, welcome centers, rest areas and the Public Service Commission offices.

Another option for expanding broadband access may be Broadband over Power Lines (BPL). The BPL option could be used to offer easier access to connect rural users to broadband technology since the power grid infrastructure already reaches these customers. The Commission is only aware of one company currently marketing BPL in Michigan. With financing from the State, this service is being implemented in two Michigan cities, Grand Ledge



<sup>12</sup> Over 200 kbps in at least one direction.

and St. Johns. This is only the fifth such commercial deployment in the nation. While the current scope of this project is limited, this is another technology that may begin to have an effect on telecommunications competition in Michigan in the future.

Wi-Max and other new technologies are in the early stages of deployment in Michigan and no information is available to report at this time. The Commission continues to monitor the emergence of new technologies and any effects they might have on wireline competition in Michigan.

### **Mergers and Acquisitions**

One area that had and will continue to have an impact on competition levels in Michigan involves industry mergers/acquisitions. On November 18, 2005, the transfer of control of AT&T Corp. and its subsidiaries to SBC Communications (subsequently named AT&T Inc.) was completed. The FCC approved the merger with conditions relating to high capacity transport services, special access pricing, unbundled network elements as well as providing digital subscriber lines<sup>13</sup> (xDSL) service on a stand-alone basis.

A merger of Verizon Communications, Inc. and MCI, Inc. was consummated on January 6, 2006. This transfer of control resulted in MCI becoming a wholly-owned subsidiary of Verizon and was renamed Verizon Business. The FCC approved this merger on November 17, 2005 with qualifications regarding special access, stand alone DSL and internet policy.

The effects of these mergers could not be determined for 2005 as the AT&T merger took place at the end of the year and the Verizon merger in January, 2006. By the next report more information should be available. Nevertheless, it should be noted that AT&T Communications, Inc. is now a subsidiary of AT&T Michigan; thus the competitive lines owned by the competitor (former/old AT&T) are now owned by the incumbent and no longer considered to be competitive

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<sup>13</sup> xDSL is a generic name for high speed digital lines provided by CLECs and ILECs to their local subscribers. These lines provide up to 8 million bits per second.



lines by the Commission for the analysis in this report. The Verizon/MCI merger was not completed until 2006 so telephone lines owned by the former MCI were reported separately for 2005 and therefore considered to be competitive lines for 2005 in this report.

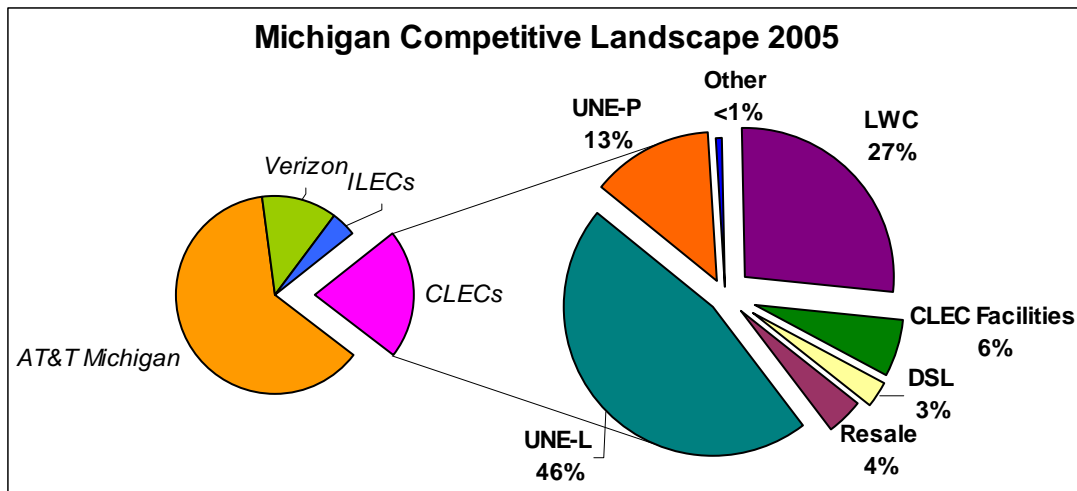
## **Conclusion**

Based on available data gathered by the Commission through its surveys over the last seven years, there was continued growth in the percentage share of CLEC lines in Michigan from a 4% share in 1999 to a 27.5% share in 2004. In 2005, that percentage declined to 21.2%, representing a 31% decline in competitive lines. The decrease in 2005 indicates that competition in the basic local exchange industry in Michigan is undergoing significant changes.

Competition for basic local exchange service in Michigan prior to 2005 was based mainly on CLECs using local switching via AT&T Michigan's UNE-P to provision customers. UNE-P accounted for 66% of the competitive lines used to serve customers in 2004 and in 2005 it decreased to 13% and will have disappeared altogether in 2006. This method of serving customers was eliminated when the FCC and the courts overturned portions of the FCC's Triennial Review Order (TRO), and eliminated the ILEC's obligation to provide UNE-P to the CLECs at a regulated, cost-based price. This is significant because the current competition level in Michigan was predominantly reached through the use of UNE-P provisioning, which accounted for a large majority of the competitive market in 2004. As a result of the FCC and court actions, Michigan is experiencing a significant change in the area of wireline competition.

This transition away from UNE-P was directed to be completed by March 11, 2006 pursuant to the timeframe set forth in the FCC's order. During 2005, the Commission actively participated in negotiations to transition customers in a timely and efficient manner. Competitive providers have transitioned customers from UNE-P to other methods; mostly using UNE-L or by

using LWC service, which competitors can purchase from AT&T Michigan at unregulated, market-based prices.



The above chart depicts the competitive landscape in Michigan for 2005 that has changed dramatically from 2004 when UNE-P accounted for 66% and UNE-L represented just 18% of the competitive landscape.

The elimination of UNE-P as a more economical method of provisioning customers, the emergence of new technology options, and the recent mergers involving incumbents and competitors have led to the decrease in competition in the wireline industry in Michigan. It should be noted that these factors are governed by outside forces, such as the FCC and courts or are affected by the introduction of new technologies into the market, and are not under the direct regulatory control of this Commission.

The Commission will continue to strive to meet its obligations under the new MTA to ensure a reasonable primary basic local exchange service rate, enforce basic consumer protections, including prohibitions against slamming and cramming, and resolve disputes that arise under the MTA. The Commission will also apprise the Governor and the Legislature of any future developments that may warrant action.